

MANAGEMENT'S DISCUSSION AND ANALYSIS

The management of the City of Lincoln, Nebraska (the City) offers readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended August 31, 2002. Please consider this discussion in conjunction with the additional information provided in the Letter of Transmittal (beginning on page viii) and the transactions, events and conditions reflected in the City's financial statements (beginning on page 16).

FINANCIAL HIGHLIGHTS

- The assets of the City exceeded its liabilities at August 31, 2002, by \$1,072,976,089 (net assets). Of this amount, \$125,959,478 (unrestricted net assets) may be used to meet the government's ongoing obligations to citizens and creditors.
- The City's total net assets increased by \$70,126,667. Of this amount \$54,675,536, or 78 percent, was an increase in governmental activities and \$15,451,131, or 22 percent, related to business-type activities.
- As of August 31, 2002, the City's governmental funds reported combined ending fund balances of \$170,547,426, an increase of \$11,161,199 in comparison with the prior year. Over half of this total amount, \$96,798,919, is available for spending at the City's discretion (unreserved fund balance).
- As of August 31, 2002, unreserved fund balance for the general fund was \$36,735,397, or 47 percent of total general fund expenditures.
- The City's total bonded debt increased by \$108,337,000 (27 percent) during the current fiscal year. The key factor in this increase was the issuance of \$141,150,000 in revenue bonds by Lincoln Electric System.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The statement of net assets presents information on all of the City's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The statement of activities presents information showing how the City's net assets changed during the year ended August 31, 2002. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City include general administrative services, public safety, streets and highways, health, planning and zoning, parks and recreation, libraries, aging services, job programs, urban development, mass transportation, engineering, self-insurance, and fleet management. The business-type activities of the City include water, wastewater and electric utilities, ambulance transport, sanitary landfill, golf courses, auditorium, and parking.

The government-wide financial statements can be found on pages 16-17 of this report.

FUND FINANCIAL STATEMENTS

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental funds – Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the City's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and government-wide activities.

The City maintains thirty-eight individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General fund, the Street Construction fund, and the Community Health Permanent Endowment fund, which are considered to be major funds. Data from the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of the nonmajor governmental funds is provided in the form of combining statements elsewhere in this report.

The City adopts an annual appropriated budget for its general fund and most other governmental funds. A budgetary comparison statement has been provided for the General and Street Construction major funds to demonstrate compliance with this budget.

The basic governmental fund financial statements can be found on pages 18-22 of this report.

Proprietary funds – The City maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses enterprise funds to account for its parking facilities and lots, golf courses, auditorium, sanitary landfill, ambulance services, wastewater, water, and electric systems. Internal service funds are used to accumulate and allocate costs internally among the City's various functions. The City uses internal service funds to account for its data processing, engineering, insurance, fleet management, telecommunications, and copy services. Because these services predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water, Wastewater and Electric Systems, all of which are considered to be major funds of the City. Data from the other enterprise funds are combined into a single, aggregated presentation. Internal service funds are also combined into a single, aggregated presentation in the proprietary fund financial statement. Individual fund data for these funds is provided in the form of combining statements elsewhere in this report.

The basic proprietary fund financial statements can be found on pages 23-25 of this report.

Fiduciary funds – Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the City's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

The fiduciary fund financial statements can be found on pages 26-27 of this report.

NOTES TO THE FINANCIAL STATEMENTS

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 30-62 of this report.

OTHER INFORMATION

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City's progress in funding its obligation to provide pension benefits to its police and fire employees. Required supplementary information can be found on page 54 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

This discussion and analysis requires focus on the current-year results in comparison with the prior year and the positive and negative aspects of this comparison. Since 2002 is the first year to report government-wide activities on the accrual basis of accounting, a comparison to the prior year is not possible in all areas of analysis. In subsequent years' reports, the current year/prior year comparisons will be displayed to enhance the reader's understanding of the City's financial position and results of operations.

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$1,072,976,089 at August 31, 2002.

By far the largest portion of the City's net assets (74 percent) reflects its investment in capital assets (e.g., land, buildings, improvements, utility plant, infrastructure, and machinery and equipment), less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

City Of Lincoln Condensed Statement of Net Assets August 31, 2002

	Governmental Activities	Business-type Activities	Total
Current and Other Assets	\$ 223,316,292	308,555,656	531,871,948
Capital Assets	372,780,466	855,103,760	1,227,884,226
Total Assets	596,096,758	1,163,659,416	1,759,756,174
Long-Term Liabilities Outstanding	82,430,754	509,299,026	591,729,780
Other Liabilities	19,897,186	75,153,119	95,050,305
Total Liabilities	102,327,940	584,452,145	686,780,085
Net Assets:			
Invested in Capital Assets,			
Net of Related Debt	321,761,052	476,054,560	797,815,612
Restricted	101,499,367	47,701,632	149,200,999
Unrestricted	70,508,399	55,451,079	125,959,478
Total Net Assets	\$ 493,768,818	579,207,271	1,072,976,089

An additional portion of the City's net assets (14 percent) represents resources that are subject to external restrictions on their use. The remaining balance of unrestricted net assets (12 percent) may be used to meet the government's ongoing obligations to citizens and creditors.

At August 31, 2002, the City is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities.

City Of Lincoln
Statement of Activities and Changes in Net Assets
Year ended August 31, 2002

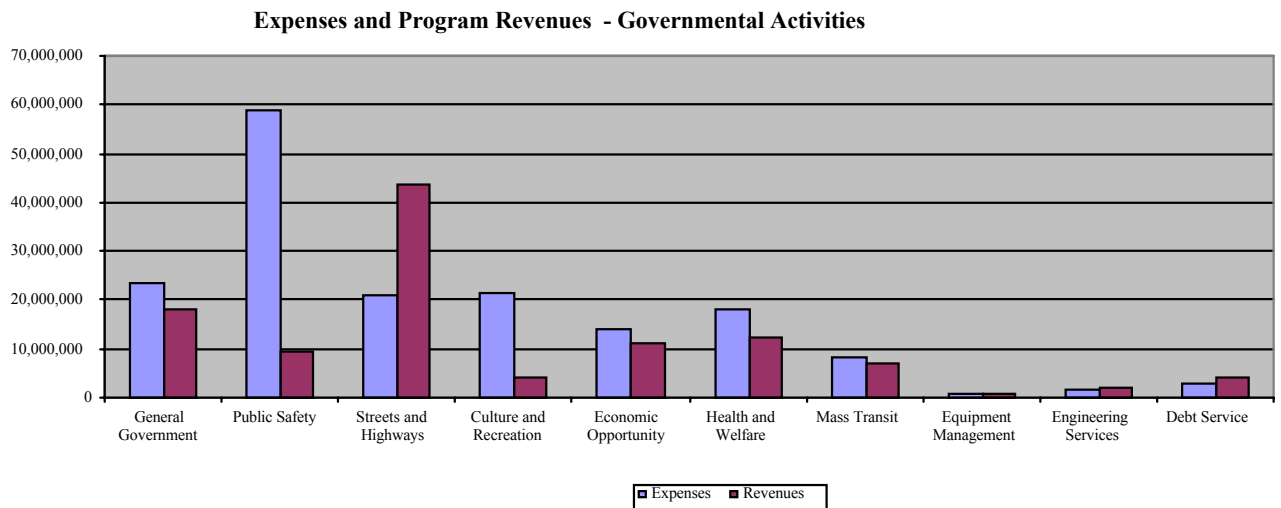
	Governmental Activities	Business-type Activities	Total
Revenues:			
Program Revenues:			
Charges for Services	\$ 33,708,219	214,711,471	248,419,690
Operating Grants and Contributions	56,861,307	3,296	56,864,603
Capital Grants and Contributions	22,629,262	6,073,286	28,702,548
General Revenues:			
Property Taxes	34,991,750	-	34,991,750
Sales and Use Tax	47,049,405	-	47,049,405
Other Taxes	20,414,161	-	20,414,161
Unrestricted Grants and Contributions	3,425,878	-	3,425,878
Investment Income	3,495,539	5,239,848	8,735,387
Other	1,407,755	353,338	1,761,093
Total Revenues	<u>223,983,276</u>	<u>226,381,239</u>	<u>450,364,515</u>
Expenses:			
General Government	23,530,070	-	23,530,070
Public Safety	58,784,389	-	58,784,389
Streets and Highways	21,073,128	-	21,073,128
Culture and Recreation	21,219,904	-	21,219,904
Economic Opportunity	14,097,457	-	14,097,457
Health and Welfare	18,133,340	-	18,133,340
Mass Transit	8,176,390	-	8,176,390
Equipment Management	906,227	-	906,227
Engineering Services	1,810,386	-	1,810,386
Interest and Fiscal Charges on Debt	2,680,738	-	2,680,738
Parking	-	3,914,224	3,914,224
Golf Courses	-	2,785,793	2,785,793
Auditorium	-	2,303,780	2,303,780
Sanitary Landfill	-	5,428,560	5,428,560
Ambulance Transport	-	3,518,764	3,518,764
Wastewater	-	12,659,850	12,659,850
Water	-	18,206,099	18,206,099
Electric	-	161,026,000	161,026,000
Total Expenses	<u>170,412,029</u>	<u>209,843,070</u>	<u>380,255,099</u>
Increase in Net Assets Before Transfers	53,571,247	16,538,169	70,109,416
Transfers	1,104,289	(1,087,038)	17,251
Increase in Net Assets	54,675,536	15,451,131	70,126,667
Net Assets 09/01/01	439,093,282	563,756,140	1,002,849,422
Net Assets 08/31/02	<u>\$ 493,768,818</u>	<u>579,207,271</u>	<u>1,072,976,089</u>

GOVERNMENTAL ACTIVITIES

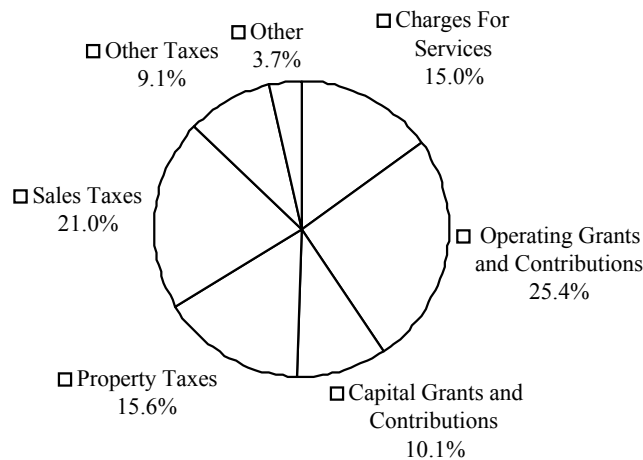
Governmental activities increased the City's net assets by \$54,675,536, accounting for 78 percent of the total growth in the net assets of the City of Lincoln. Key elements of this increase are as follows:

- Property taxes increased by approximately \$2.1 million (6 percent) during 2002. Adjustments were made to property values to comply with state guidelines regarding the relationship of taxable valuations to market value. The value created by new growth (improvements, new construction, additions of new property, and annexations) in the tax base was 4.3%, prior to the revaluation of property. Total growth in the tax base, which includes revaluations and other adjustments, was 11.5%.
- Net sales and use tax increased by approximately \$3.1 million (7.0 percent) during 2002. A significant factor in this increase was a 27.5 percent reduction in the amount of sales and use taxes that were refunded pursuant to a business expansion incentive program created by State law. Gross sales and use tax, which is the amount collected before the business incentive refunds, increased by 4.6 percent during 2002. This percentage increase more closely mirrors the economic growth within the City during 2002.

- Operating and capital grants increased as a result of several major construction projects receiving state and federal funding and an aggressive grant application strategy undertaken during 2002.
- For the most part, increases in expenses closely paralleled inflation and growth in the demand for services. One noteworthy exception was the City's highways and streets program. The growth in expenses reflects the City's decision to change its policy regarding the letting of construction projects. Previously, the policy was to delay letting of contracts until adequate cash was on hand to pay for the contract. The current policy is to award contracts when the resources have been secured even if some of the resources are received in subsequent periods.



Revenues By Source - Governmental Activities

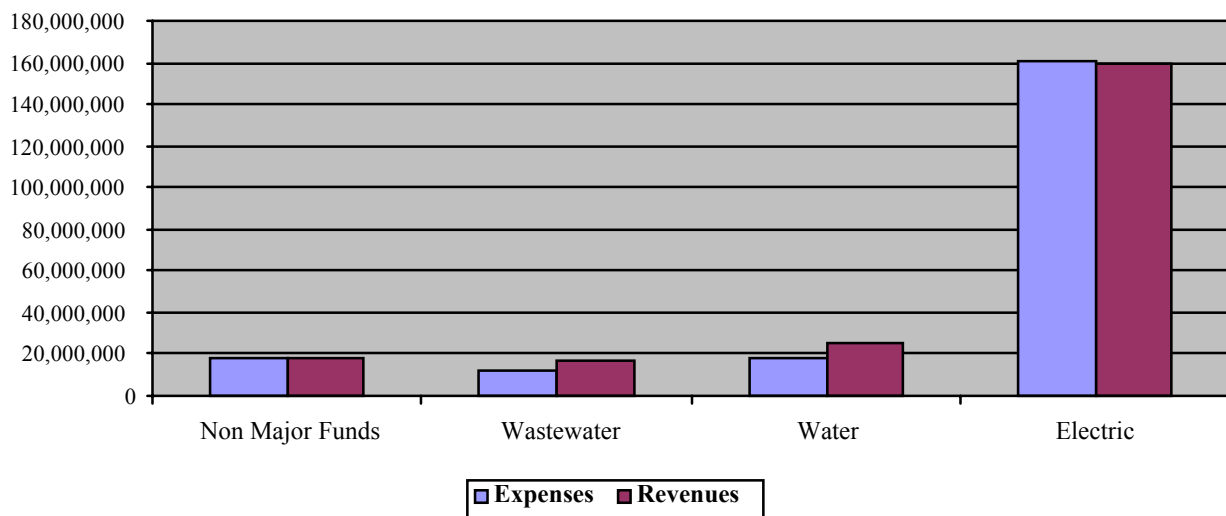


BUSINESS-TYPE ACTIVITIES

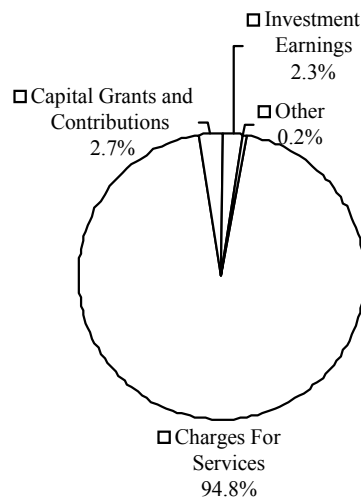
Business-type activities increased the city's net assets by \$15,451,131, accounting for 22 percent of the total growth in the government's net assets. Key elements of this increase are as follows:

- Charges for services increased by approximately \$5.5 million, or 3 percent. The Water System accounts for a significant portion of this increase, largely due to increased water usage related to the severe drought conditions experienced by Nebraska this past year. In June 2002, the Mayor of the City of Lincoln asked the customers of the System to voluntarily comply with alternate day watering restrictions, which became mandatory a month later. These restrictions lasted into September 2002. Revenues also increased for the Electric System due to 22% higher wholesale revenue from an increase in wholesale sales.
- Capital Contributions were an increased revenue source for the Water System as the result of significant construction activity during the year.

Expenses And Program Revenues - Business-type Activities



Revenues By Source - Business-type Activities



FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

GOVERNMENTAL FUNDS

The focus of the City's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the City's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of August 31, 2002, the City's governmental funds reported combined ending fund balances of \$170,547,426, an increase of \$11,161,199 in comparison with the prior year. Of this total amount, 57 percent constitutes unreserved fund balance, which is available for spending at the City's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed to:

- liquidate contracts and purchase orders of the prior period (\$20,838,111),
- pay debt service (\$12,630,821),
- generate income for the purpose of funding health and health-related programs for the citizens of Lincoln (\$37,000,000), and
- a variety of other restricted purposes (\$3,279,575).

The General Fund is the chief operating fund of the City. At August 31, 2002, the unreserved fund balance of the general fund was \$36,735,397, while total fund balance reached \$38,131,061. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 47 percent of total general fund expenditures, while total fund balance represents 49 percent of that same amount.

The fund balance of the City's general fund increased by \$2,443,129 during 2002. Due to a weakening economy at the federal and state level, plus a slowing of the growth rate of the City's sales tax revenues, several steps were taken early in the year that resulted in reductions of General fund expenditures. These steps included a:

- freeze on certain capital improvement projects funded with General funds,
- temporary hiring freeze that delayed the filling of approximately 30 positions,
- temporary travel freeze that saved approximately \$72,000 when comparing budget to actual dollars spent.

The Street Construction fund had a total fund balance of \$22,840,924, which is to be used in the construction and maintenance of street and highways. The net decrease in fund balance during 2002 in the Street Construction fund was \$3,058,635. This decrease was anticipated as a result of the Public Works department's strategy to increase its capital construction program and to implement the acceleration of the awarding of construction contracts.

PROPRIETARY FUNDS

The City's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

Unrestricted net assets of the Wastewater System, Water System, Electric System, and other enterprise funds amounted to \$14,798,667, \$8,703,342, \$29,226,000 and \$2,723,070, respectively, at August 31, 2002. Factors concerning the finances of these funds have already been addressed in the discussion of the City's business-type activities.

GENERAL FUND BUDGETARY HIGHLIGHTS

Differences between the original budget and the final amended budget were relatively minor (decrease of \$74,416 in appropriations) and can be briefly summarized as follows:

- \$(120,526) in miscellaneous decreases in general government activities.
- \$22,500 in increases allocated to traffic engineering.
- \$23,697 in increases allocated to street maintenance.
- \$(208,000) in decreases allocated to parks and recreation.
- \$207,913 in increases allocated for general fund transfers to other City funds.

Variances between actual General fund revenues and expenditures and the final amended budget included the following:

- \$2,913,599 positive variance in property taxes. Actual property tax collections were 96% for the 2001 levy, while estimated tax revenue is based on 90% collections as provided by the City Charter.
- \$(2,068,594) negative variance in sales taxes. Projected collections for 2002 reflect a 6.7% increase over prior year collections, while 2002 actual collections on a budget basis increased by only 2% due to refunds and a slowing economy.
- \$1,485,807 positive variance in occupation taxes. Actual collections include the receipt of underpayments of the telecommunications tax in prior years.
- \$2,283,552 positive variance in general government/miscellaneous function expenditures. This variance was the result of better than anticipated insurance costs, delayed expenditures when possible in anticipation of reduced revenues, and contingency funds left unspent.

CAPITAL ASSET AND DEBT ADMINISTRATION

CAPITAL ASSETS

The City's investment in capital assets for its governmental and business-type activities as of August 31, 2002, amounts to \$1,227,884,226 (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements, machinery and equipment, streets, bridges, storm sewers, electric plant, and water and sewer plant. The total increase in the City's investment in capital assets for 2002 was 8 percent (a 14 percent increase for governmental activities and a 6 percent increase for business-type activities).

Major capital asset events during 2002 included the following:

- Construction was completed on two new library facilities; current year expenditures were \$1,579,702.
- Construction was completed on a new swimming pool; current year expenditures were \$1,672,458.
- Construction was completed on a new community recreation center; current year expenditures were \$1,449,845.
- 20 new buses were added to the City's bus system at a value of \$5,107,150.
- A variety of street construction widening and expansion projects for existing streets and bridges began; construction-in-progress as of August 31, 2002, reached \$55,410,408. Current year expenditures for street construction right-of-way were approximately \$6,012,000.
- The utility plant increase represents the completion of the Rokeby 3 unit (a simple cycle industrial-frame peaking unit). The design and construction of the Salt Valley Generating Station began in 2001 and will be commercial in 2003.
- Wastewater System anaerobic digester modifications and improvements; construction-in-progress as of August 31, 2002, is \$3,305,930.

- Wastewater System aeration system improvements; construction-in-progress as of August 31, 2002, is \$2,780,457.
- Construction of a 10 million gallon water storage reservoir; construction-in-progress as of August 31, 2002, reached \$3,393,317.
- Major modification to existing Water System pumping facilities; the asset was placed in service during 2002 at a total cost of \$3,256,910.
- Construction of new and replacement water distribution mains and related projects; construction-in-progress as of August 31, 2002, reached \$8,423,251.
- Construction of a softball complex, through the partnership of the City, University of Nebraska, and a private investor, was completed in the current year. Ownership of the facilities passed to the City through a lease arrangement with the University and the private investor. Total value of the softball complex was recorded at \$3,000,000. The related baseball complex was recorded as an asset in 2001.

City Of Lincoln
Capital Assets (net of depreciation)
August 31, 2002 and 2001

	Governmental Activities		Business-type Activities		Total	
	2002	2001	2002	2001	2002	2001
Land	\$ 37,810,841	30,992,503	14,185,253	13,592,178	51,996,094	44,584,681
Buildings	42,017,061	27,384,764	123,066,708	120,649,382	165,083,769	148,034,146
Improvements Other Than Buildings	31,967,261	27,765,012	225,201,069	215,839,899	257,168,330	243,604,911
Machinery and Equipment	29,958,223	23,025,302	10,731,801	10,493,886	40,690,024	33,519,188
Utility Plant	-	-	396,247,000	363,635,000	396,247,000	363,635,000
Infrastructure	171,464,392	166,198,108	-	-	171,464,392	166,198,108
Construction-in-progress	59,562,688	50,397,524	85,671,929	84,564,371	145,234,617	134,961,895
Total	\$ 372,780,466	325,763,213	855,103,760	808,774,716	1,227,884,226	1,134,537,929

Additional information on the City's capital assets can be found in Note 7 of the notes to the financial statements on pages 43-45 of this report.

LONG-TERM DEBT

At August 31, 2002, the City of Lincoln had total bonded debt outstanding of \$504,645,000. Of this amount, \$56,687,000 comprises debt backed by the full faith and credit of the City and \$310,000 is special assessment debt for which the government is liable in the event of default by the property owners subject to the assessment. The remainder of the City's debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds).

City Of Lincoln
Outstanding Bonded Debt
(dollar amounts in thousands)
August 31, 2002 and 2001

	Governmental Activities		Business-type Activities		Total	
	2002	2001	2002	2001	2002	2001
General Obligation Bonds	\$ 56,687	53,998	-	-	56,687	53,998
Special Assessment Debt With						
Governmental Commitment	310	420	-	-	310	420
Tax-supported Revenue Bonds	11,080	-	-	-	11,080	-
Revenue Bonds	-	-	436,568	341,890	436,568	341,890
Total	\$ 68,077	54,418	436,568	341,890	504,645	396,308

The City's total debt increased by \$108,377,000 (27 percent) during 2002. The key factor in this increase was a \$141,150,000 revenue bond issuance for the City's electric system to fund construction of the Salt Valley Generating Station. The City also issued \$7,500,000 in storm sewer bonds to finance drainage improvements in existing residential areas; \$11,080,000 in tax-supported Antelope Valley project bonds; \$6,000,000 in parking revenue bonds issued primarily for construction of the City's Haymarket parking garage.

During 2002, the City issued revenue refunding bonds to refinance previously outstanding golf course revenue bonds to take advantage of favorable interest rates. The result is expected to be a decrease in future debt service payments of \$600,533.

In addition, \$35,510,000 in outstanding Lincoln Electric 1992 Series A bonds were refunded with taxable commercial paper notes. LES advance refunded the 1992 bonds to restructure its debt and to provide for more flexible covenants and improve business operation.

The City maintains the following credit ratings:

	Moody's Investors <u>Service</u>	Standard And <u>Poor's</u>	Fitch Investors <u>Service</u>
General Obligation Bonds	Aa1	AAA	
Municipal Infrastructure			
Redevelopment Fund Bonds	Aa2	AAA	
Water Revenue	Aa2	AA+	
Parking Revenue	A2	A	
Electric Revenue:			
1993 Bonds	Aa2	AA+	AA
1998 Bonds	Aa2	AA	AA
2001 Bonds	Aa2	AA	AA
Commercial Paper – tax exempt		A1+	F1+
Commercial Paper – taxable	MIG 1	A1+	F1+

Under the City's Home Rule Charter, there is no legal debt margin.

Additional information on the City's long-term debt can be found in Note 9 of the notes to the financial statements on pages 46-51 of this report.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

- The increase in the City's property tax base provided by real growth is estimated at 3.2% for 2003. Total growth, including revaluations of current property, is estimated at 3.8%
- Sales tax collections have increased by 2% over each of the past two years, with current collections through January 2003 also showing an increase over the same period in 2002. The sales tax base has been expanded by the Nebraska Legislature to include certain services. Sales tax collections have been negatively impacted by slowing economic growth and record high rate of refunds which are part of the business incentives provided by State law.
- Current overall revenue growth is projected to slow to less than 2%.

All of these factors were considered in preparing the City's budget for the 2003 fiscal year.

During 2002, unreserved fund balance in the general fund increased to \$36,735,397. The City of Lincoln anticipates appropriating \$6,111,631 of this amount for spending in the 2003 fiscal year budget. It is intended that this use of available fund balance will avoid the need to raise property taxes during the 2003 fiscal year.

The water and electric utility rates were increased for the 2003 budget year. The water rates were increased by 7 percent while the average increase in the electric rates was 4 percent. The rate increases affected both residential and industrial consumers by approximately the same percentage. These increases are necessary to fund debt service on the new debt issued by the utilities.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City of Lincoln's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City of Lincoln, Finance Department, 555 South 10th Street, Lincoln, NE 68508.